



State of Washington  
Department of Revenue

# Excise Tax Advisory

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## WATER CONDITIONING SERVICES

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Is the business of providing deionized and softened water by way of portable exchange tanks which must be periodically cleaned and regenerated by the taxpayer's employees a service or a lease of tangible personal property?

The taxpayer, a Culligan Water Conditioning franchise dealer, offered two distinct types of water softening equipment to customers. The first was a complete softener unit which continuously regenerated the ion-exchange material within itself and regularly provided soft water once installed in the customer's plumbing system. This "automatic unit" was sold or rented to the customer who operated and serviced the unit himself. The taxpayer collected retail sales tax from its customers on the sale or lease of "automatic units" and such tax was not in issue.

The second type, called an "exchange unit," was the subject of the controversy. This unit, once installed in the customer's plumbing, also regularly provided soft water but unlike the "automatic unit" cannot itself regenerate the ion-exchange material. The customer would contract with the taxpayer and the latter would provide the exchange unit, connect it to the customer's water system, and periodically replace the ion-exchange material in the unit in order to maintain a continuous flow of softened water. The taxpayer would service the unit by removing the exchange tank at the customer's location, replace it with new or regenerated material, and regenerate the old tank at its plant. Over the years, in line with Department of Revenue instructions, the taxpayer reported this income under the Service business and occupation tax classification and paid sales or use tax on all equipment and supplies used in conjunction with the "exchange units."

***ETBS have been made Excise Tax Advisories, and have retained their old number. Advisories with a 2 (plus three digits) are new advisories, ETBs that have been revised and readopted after review under the Department's regulatory improvement program, or advisories that have been revised and/or readopted.***

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Please direct comments to:  
Department of Revenue  
Legislation & Policy Division  
P O Box 47467  
Olympia, Washington 98504-7467  
(360) 753-4161 eta@DOR.wa.gov

The lease of tangible personal property for excise tax purposes is a retail sale (RCW 82.04.050). The Department believes that, in light of RCW 82.04.050 and a recent California Supreme Court decision precisely on point, *Culligan Water Conditioning of Bellflower, Inc. v State Board of Equalization*, 17 Cal 3d 88, 55 P2d 593 (1976), it is clear that the taxpayer is renting tangible personal property in providing exchange units to its customers and that all of its income from this activity is subject to retail sales tax.

In the above-cited case, the Court ruled that the true object of the water conditioning contract was the furnishing of the exchange unit which, by itself and without requiring any performance of human labor, softened the water. The Court recognized that even though human labor or service was involved in regenerating the ion-exchange material, nevertheless, the customer's purpose was to obtain, not personal services, but a properly generated and efficiently functioning water conditioning unit.

The same conclusion is evident when applying this rationale to sales made by Culligan dealers in Washington. The customer in a very practical sense has the use of the exchange unit which is installed in his plumbing system and has dominion and control over it while it is there. The customer uses the exchange unit by having the water pass along the lead-in pipes, through the conditioning unit, and thereafter throughout the entire water system of his residence. The customer may activate the unit and avail himself of its functioning by the simple act of turning on a faucet, or he may permit it to remain inactive simply by not using the water, as he might do during long absences during the day, or over many days while away from home, or during long hours of nonuse during the night. The fact that the taxpayer has an owner's control of the unit and the exclusive right to replace one unit with another so as to regenerate the exhausted material at its plant, does not derogate in any way from the customer's right to use and control the unit while it is on his premises. The water softening is done by the water conditioning unit and the taxpayer's service of generating and installing is merely incidental to the function performed by the unit. It is therefore a lease of tangible personal property.

The Department recognized that to apply the retail sales tax to all past transactions would cause an undue hardship upon the taxpayer. It therefore instructed the taxpayer and all similarly situated water conditioning dealers to report the gross income from the sale or lease of exchange units under the Retailing classification and to collect retail sales tax beginning on January 1, 1981.